



# McDonald's Corporation(MCD)

Updated April 8<sup>th</sup>, 2018 by Jonathan Weber

## Key Metrics

<b>Current Price:</b> \$161	<b>5 Year CAGR Estimate:</b> 7.2%	<b>Quality Percentile:</b> N/A
<b>Fair Value Price:</b> \$152	<b>5 Year Growth Estimate:</b> 5.9%	<b>Momentum Percentile:</b> N/A
<b>% Fair Value:</b> 106%	<b>5 Year Valuation Multiple Estimate:</b> -1.2%	<b>Total Return Percentile:</b> N/A
<b>Dividend Yield:</b> 2.5%	<b>5 Year Price Target</b> \$202	<b>Valuation Percentile:</b>

## Overview & Current Events

McDonald's is the largest publicly traded restaurant company in the world. McDonald's, which was founded in 1940, has a market capitalization of \$130 billion. The company has a long dividend growth history, which has made it a favorite holding for many retail investors.

During Q4 2017 McDonald's earned \$1.71 per share, an increase of 19% year over year. Revenues were down by 11%, which is due to the company's refranchising strategy; to have fewer company owned stores and more franchised locations. Comparable store sales at the company, which are an important driver for higher profits, were up by a super-sized 5.5% during the most recent quarter.

Results in fiscal 2017 results were excellent as well, earnings per share grew 17% year-over-year and comparable store sales were up by 5.3%, widely outperforming the industry.

## Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
<b>EPS</b>	\$3.67	\$3.98	\$4.60	\$5.27	\$5.36	\$5.55	\$4.82	\$4.97	\$5.71	\$6.66	<b>\$7.60</b>	<b>\$10.10</b>
<b>DPS</b>	\$1.63	\$2.05	\$2.26	\$2.53	\$2.87	\$3.12	\$3.28	\$3.44	\$3.61	\$3.83	<b>\$4.10</b>	<b>\$5.50</b>

McDonald's has a long and successful growth history, but a couple of years ago they took a small step back. McDonald's has found ways to reignite growth, though, which included driving comps sales by offering all day breakfast at its restaurants and expanding the menu (organic meat, healthier alternatives). Another big strategic shift was McDonald's decision to refranchise many of its restaurants. The company records a lower amount of revenues now, but costs have come down as well. McDonald's has turned itself into an asset-light, low-cost company that collects franchise fees from a huge number of restaurants (and operates a smaller number of restaurants itself).

This strategy has been very successful, as EPS have grown at a strong pace over the last three years. It seems highly likely that McDonald's will continue to perform well in the future, as EPS growth will be driven by higher franchising fees, lower costs and the impact of share repurchases.

## Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
<b>Avg. P/E</b>	15.8	14.4	15.4	15.9	17.3	17.5	20.0	20.2	21.1	22.3	<b>21.2</b>	<b>20.0</b>
<b>Avg. Yld.</b>	2.8%	3.6%	3.2%	3.0%	3.1%	3.2%	3.4%	3.4%	3.0%	2.6%	<b>2.5%</b>	<b>2.7%</b>

McDonald's valuation has expanded significantly over the last decade, which isn't a big surprise since shares were trading at a rather inexpensive valuation in the past. As the broad market's valuation multiple has risen, so has McDonald's. The valuation has come down slightly so far in 2018, but is still close to the ten-year high. Going forward some multiple contraction seems more likely than multiple expansion from the current level.

McDonald's dividend yield of 2.5% isn't as high as it used to be, but still significantly above the broad market's 1.8% dividend yield.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
<b>GP/A</b>	30.2%	29.3%	30.1%	32.4%	30.5%	29.8%	30.7%	25.9%	32.9%	31.4%	<b>31.0%</b>	<b>32.0%</b>
<b>Debt/A</b>	53.0%	53.6%	54.1%	56.4%	56.8%	56.3%	62.6%	81.5%	107%	109%	<b>110%</b>	<b>110%</b>
<b>Int. Cov.</b>	12.8	15.3	17.3	17.2	16.6	16.5	13.9	11.3	8.8	10.3	<b>10.5</b>	<b>11.0</b>
<b>Payout</b>	44.4%	51.5%	49.1%	48.0%	53.5%	56.2%	68.0%	69.2%	63.2%	57.5%	<b>53.9%</b>	<b>54.5%</b>
<b>Std. Dev.</b>	33.9%	22.5%	15.4%	16.7%	14.2%	11.9%	12.8%	19.4%	15.0%	13.2%	<b>15.0%</b>	<b>15.0%</b>

The start of McDonald's refranchising efforts is clearly visible in the above table, as the lower amount of assets held has led to a rise in the gross profit to assets ratio a couple of years ago. At the same time the company's asset base shrunk, McDonald's has taken on billions of debt (to finance the company's shareholder returns, mainly via share repurchases). This has made the debt to assets ratio rise above 100%, but since interest coverage is still very solid at more than ten, the debt level is not a reason to worry.

McDonald's global scale makes the company less vulnerable to headwinds in one geographic region, and the company has managed to differentiate itself from most of the other restaurant operators: McDonald's has reported strong comps sales for the last two years, whereas the restaurant industry as a whole suffered from declining comps. With its rather inexpensive offerings McDonald's is also relatively recession-proof, during the 2008-2009 financial crisis McDonald's earnings kept increasing.

The payout ratio jumped up a couple of years ago (when McDonald's earnings declined in 2014 and they still increased the dividend), but has been coming down since. Due to a strong earnings growth outlook McDonald's should be able to grow the dividend easily whilst the payout ratio remains in the mid-50% range.

## Final Thoughts & Recommendation

McDonald's provides a 2.5% dividend yield, which is high relative to what the market as a whole is offering. Shares of McDonald's are not cheap, but not overly expensive either, and due to a solid growth outlook shareholders should benefit from attractive total returns going forward.

McDonald's has been a low-risk investment that provides rising dividends in the past, and it will remain the same going forward.

## Total Return Breakdown by Year

